STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

Illinois Bell Telephone Company	)	
	)	**Docket No. 98-0252**
Application for Review of Alternative Regulation Plan	)	
Illinois Bell Telephone Company	)	
	)	**Docket No. 98-0335**
Petition to Rebalance Illinois Bell Telephone Company's Carrier Access and Network Access Line Rates	)	
Citizens Utility Board, People of the State of Illinois	)	**Docket No. 00-0764**
v.	)	
Illinois Bell Telephone Company	)	**(Consol.)**

APPLICATION FOR REHEARING OF SBC ILLINOIS

Louise A. Sunderland
Karl B. Anderson
Mark A. Kerber
Illinois Bell Telephone Company
225 West Randolph Street, Floor 25D
Chicago, Illinois 60606
(312) 727-6705
(312) 727-2928
(312) 727-7140

Dated: January 29, 2003

TABLE OF CONTENTS

STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION

Illinois Bell Telephone Company **Application for Review of Alternative Regulation Plan**	))))	**Docket No. 98-0252**
Illinois Bell Telephone Company **Petition to Rebalance Illinois Bell Telephone Company's Carrier Access and Network Access Line Rates**	)))))	**Docket No. 98-0335**
Citizens Utility Board, People of the State of Illinois **v.** **Illinois Bell Telephone Company**	))))	**Docket No. 00-0764** **(Consol.)**

APPLICATION FOR REHEARING OF SBC ILLINOIS

Illinois Bell Telephone Company ("SBC Illinois" or the "Company"), by its attorneys, hereby submits its Application for Rehearing of the Commission's Order in the above-captioned proceeding, dated December 30, 2002 (the "Order").

INTRODUCTION

In 1994 this Commission substituted the Alternative Regulation Plan for traditional rate base/rate of return regulation for SBC Illinois under Section 13-506.1 of the Public Utilities Act, which permits use of alternative means of regulation. Order, Ill. C.C. Dkts. 92-0448 & 93-0239 (October 11, 1994) (the "1994 Alt Reg Order"). Under this Plan, SBC Illinois' noncompetitive service rates are governed by a price index.[1] The index sets prices based on the level of inflation in the overall economy each year, less a

[1] Under Section 13-502 of the Public Utilities Act, telecommunications carriers' services are classified as "competitive" or "noncompetitive" based on the availability of competitive alternatives in the marketplace. Competitive services remain regulated, but are permitted greater pricing freedom.

productivity offset. The Plan also contains a service quality provision (the "Q" factor), which imposes penalties on SBC Illinois if its retail service quality falls below designated threshold or "benchmark" levels.[2] Because inflation has been low, the Plan has required substantial rate reductions each year since 1994. (Am. Ill. Ex. 1.1, p. 68).

This review proceeding was initiated in 1998 to assess the overall workings of the Plan over its first five years and to determine whether the Plan should be modified on a going-forward basis. The proceeding was held in abeyance for almost two years pending the completion of the Commission's review of the proposed SBC/Ameritech merger. A record was then developed over the course of calendar year 2000 – over two years ago. Much has changed since then, and the Commission should take these changes into consideration in evaluating the record evidence and the issues raised below by SBC Illinois.

The Commission's Order in this proceeding resolves a wide range of important issues and, to a significant degree, resolves them appropriately. However, the Order errs in several major areas.[3] *First*, the Order imposes an infrastructure investment commitment on SBC Illinois which is clearly unlawful and for which there is *no* basis in the record. *Second*, the service quality penalties have been increased to punitive levels, and such increases are not supported by the record or sound public policy. *Third*, the Commission unlawfully imposes the wholesale service remedy plan adopted in Docket

---

2 In addition, the index calculations take into account any so-called "exogenous changes," which capture cost or revenue changes which impact telecommunications carriers disproportionately as compared to companies in the economy as a whole.

3 It is well established that the Commission's decisions must be based on substantial evidence in the record. 220 ILCS 5/10-201(e)(iv)(A). Decisions not supported by substantial evidence are arbitrary and capricious and will be set aside on appeal. See, e.g., Choate v. Ill. Comm. Comm., 309 Ill. 248, 257 (1923). The Commission's orders will also be reversed on appeal if they are inadequately explained, beyond the Commission's authority, or contrary to state or federal law. 220 ILCS 5/10-201(e)(iii), 5/10-201(e)(iv)(B)-(C).

No. 01-0120 on SBC Illinois, at least on an interim basis pending completion of Docket No. 01-0662. In addition, SBC Illinois asks the Commission to reconsider its decisions on the construct of the "baskets" to which services are assigned for purposes of the Plan and its decision to reinitialize the API/PCIs which govern the required rate changes in each basket.

ARGUMENT

I. THE ORDER'S CAPITAL SPENDING REQUIREMENT IS UNLAWFUL

In the Order's concluding section, the Commission adopts a capital spending requirement that would extend merger condition that requires SBC Illinois to invest $3 billion in its network infrastructure (Merger Condition 7), by adding an additional obligation to spend $1.2 billion in 2006 and 2007, and $600 million each year thereafter, until an order continuing or terminating the Plan is adopted. Order at 211-12.[4] This requirement is clearly unlawful and is not supported by any record evidence at all.

A. THE COMMISSION CANNOT UNILATERALLY EXTEND MERGER CONDITION 7

The Commission is not free to extend Merger Condition 7 unilaterally. To the contrary, the Commission is estopped from doing so.

The doctrine of estoppel operates against public bodies where there is "an affirmative act on the part of the public entity and the inducement of a substantial reliance by the affirmative act." Gersch v. Illinois Dept. of Professional Regulation, 308 Ill. App. 3d 649, 660 (1st Dist. 1999). Estoppel applies to the situation presented here: where an agency approves action by a private party, then tries to change the rules after

[4] The five-year term of Merger Condition 7 actually runs from 2000 through 2004, not through 2005 (which would be a sixth year). Compare Order at 211-12 with Merger Order at 240. This error in the Order does not affect SBC Illinois' position.

that party has taken the action and incurred expense in reliance on the agency's approval.[5]

The Commission's 1999 order approving the merger was an affirmative act sufficient to induce the Joint Applicants to accept the merger conditions, to consummate the merger, and to implement the associated conditions, including Condition 7. The Commission stated that it would approve the SBC/Ameritech merger, provided that the Applicants agreed to the merger conditions for specified, limited durations. Order, Ill. C.C. Dkt. 98-0555 at 239-60 (September 23, 1999) (the "Merger Order"). For example, Condition 7 applies for a term five years. Id. at 240. In reliance on that order, the Joint Applicants completed the merger of two multistate, multi-billion dollar telephone companies and implemented Condition 7 (and other merger conditions) – all at considerable expense. Plainly, the duration of the merger conditions was a critical factor in that decision. After representing, in the Merger Order, that merger approval required SBC Illinois to implement Condition 7 for a limited term of five years, the Commission is not free to unilaterally alter that term. See Hickey v. Illinois Central R.R. Co., 35 Ill. 2d 427, 448-49 (1966) (estoppel will apply when there have been "positive acts by [State] officials which may have induced the action of the adverse party under circumstances where it would be inequitable to permit [that party] to stultify itself by retracting what its

[5] In Drury Displays, Inc. v. Brown, 306 Ill. App. 3d 1160 (5th Dist. 1999), for example, a property owner sought approval from the Department of Transportation to place an outdoor billboard on its property. The Department granted approval, and the property owner accordingly removed the building that had stood on the property and raised the billboard. Months later, the Department decided that the billboard was unlawful and ordered the property owner to take it down. The trial court issued a writ of mandamus enjoining the Department's action, and the Appellate Court affirmed. As the court explained, the Department's previous orders granting the requested permit were sufficient to induce the plaintiff to take action in reliance on those orders. The court found that the plaintiff, by spending approximately $50,000 to demolish the existing building and construct the billboard, incurred substantial expense in reliance on the Department's action, and accordingly "would suffer a substantial loss if the permits were not reissued." As a result, the Department was estopped from changing its position.

officers had previously done"); People v. Hill, 75 Ill. App. 2d 69, 75 (1st Dist. 1966) (holding that estoppel operated where "it was the affirmative action by the public authorities . . . that caused plaintiff to change its position by making great expenditures which would not have been made but for the affirmative action").

The Public Utilities Act (the "Act") compels the same result. By extending the duration of Condition 7, the Commission in essence created a new merger condition – that SBC Illinois spend an additional $1.2 billion in 2006 and 2007, many years after the merger closed. But Section 7-240(f) of the Act (under which the Commission imposed Condition 30 in the Merger Order) governs *when* the Commission may impose merger conditions. That section authorizes the Commission to impose "terms, conditions or requirements" *only* "[i]n approving any proposed reorganization pursuant to this Section." Section 7-204 by its plain terms applies only when a proposed reorganization is pending. It precludes the Commission from imposing new conditions after a reorganization has been consummated. Thus, the Order's capital spending requirement is unlawful.

B. NO RECORD EVIDENCE SUPPORTS THE CAPITAL SPENDING REQUIREMENT

Regarding the record, there is little to be said. This extension of the Merger Order's $3 billion capital spending requirement, as imposed by the Order, was never discussed by *any* witness or by *any* party at *any* time in this proceeding. There is literally no evidence to support it. The requirement is, therefore, clearly unlawful for that reason, too. 220 ILCS 5/10-103, 5/10-201(e)(iv)(A).

The Commission cites only the testimony of Ms. TerKeurst in support of its conclusion. The Order states: "According to Ms. TerKeurst, the $3 billion investment specified under the Merger Order is the minimum investment required to support AI's own basic products and services and should be maintained. . . . We agree." Order at 211. However, Ms. TerKeurst was *not* recommending that the $3 billion infrastructure obligation be extended in this proceeding. Instead, she proposed an entirely different capital spending obligation, *i.e.*, a dollar value per access line which would have to be spent in a designated capital account (the Wire and Cable account). The Commission *rejected* Ms. TerKeurst's capital spending proposal, finding as follows:

> "We reject GCI/City's proposal to have SBC Illinois invest at least $29 per access line annually, in the "Wire and Cable" account. The GCI/City has not established that this level of spending is reasonable or appropriate on a forward-looking basis. It simply reflects the amount that SBC Illinois spent in 1996." Order at 205.

It is arbitrary and capricious for the Commission to reject Ms. TerKeurst's specific proposal because it lacks support – and it clearly did – and then to adopt another spending proposal that was never addressed in the record at all. There is absolutely nothing in the record of this proceeding that suggests that spending $1.2 billion over 2006 and 2007 is "reasonable or appropriate on a forward-looking basis" and it cannot be adopted for the same reason that Ms. TerKeurst's proposal could not be adopted.

SBC Illinois' original commitment to spend $3 billion over the first five years of the Plan was just that – a voluntary commitment. 1994 Alt Reg Order at 191-92. As the Commission is aware, Merger Condition 7 represented a regulatory agreement by Ameritech, SBC and the Commission in Docket 98-0555, based on a full consideration of the facts and circumstances that prevailed at the time of this agreement. Merger Order at 18-19; 260 (Condition 32 required SBC and Ameritech to indicated their acceptance of the conditions). SBC Illinois made no such voluntary commitment in this proceeding, nor was the extension of the $3 billion infrastructure investment obligation agreed by the

Company. In the absence of SBC Illinois' willingness to undertake such an obligation, and lacking any record whatsoever on this issue, the Commission could not impose such an obligation on SBC Illinois, even if it were otherwise lawful.

C. Imposition Of Arbitrary Investment Obligations Is Poor Public Policy And Is Not Authorized By The Public Utilities Act

Imposition of a rigid and arbitrary investment obligation on SBC Illinois is also poor public policy. As noted above, no record been developed to show that $1.2 billion over 2006 and 2007 is the "right" level of investment, or that $600 million would be the "right" level of investment in any subsequent year. Nor would it be possible to support those conclusions.

The telecommunications industry is in severe economic difficulty, and the future structure of the industry is uncertain. No one – not the Commission and not the Company – can predict today what level of spending will be necessary or appropriate in 2006, 2007 and beyond. In fact, arbitrary spending obligations can be counterproductive and harm the very ratepayers the Commission is trying to protect. The capital markets judge companies harshly if they make investments that are not economically prudent in light of economic conditions and the needs of the business. Arbitrary investment obligations can, over the long run, saddle a company with unproductive plant, ultimately compromising its ability to attract capital and provide high quality service to its customers.

The Order would "lock in" predetermined levels of investment, which would not reflect the business and technological changes that ultimately determine how much money the Company should invest, what investments should be made, and when. Those are business decisions that must be made by the Company's management, based on the needs of the business. Nothing in the Act permits the Commission to usurp management's authority to make those decisions. Commerce Comm'n ex rel. East St. Louis, C & W Ry. v. East St. Louis & Carondelet Ry. Co., 361 Ill. 606, 616 (1935).

Moreover, the Commission has not provided any legitimate policy reasons for this investment obligation – whether inside or outside the record. The Commission's Order first suggests that investments in the network are required to satisfy statutory goals such as "innovation" and the "broad dissemination of technical improvements that reaches all classes of customers." Order at 211. As the Commission states: "As we see it, innovation is spurred by ideas and money." Id. The issue here, however, is not *whether* SBC Illinois should invest in its network. The Company spends very substantial amounts of money every year maintaining and updating its network and no one has even suggested – much less demonstrated – that these investments will cease. The issue is *how much* should be invested in any one year or over any period of time. There is no evidence whatsoever that the particular level of spending mandated by the Merger Order is required to ensure "innovation" or the "broad dissemination of technical improvements."

The Commission's concern here appears to be an extension of its findings earlier in the Order that SBC Illinois failed to sufficiently innovate during the first term of the Plan, particularly with respect to advanced services:

> "For instance, Ameritech has been very slow to deploy advanced services technology and even chose to suspend deployment of network upgrades necessary to support these services. The Commission believes that advanced services capability is critical to the economic development of Illinois and does not take lightly threats against that potential development. While Ameritech claims that innovation depends on equipment manufacturers, it ignores this example where Ameritech intentionally elected not to employ technology already developed." Id. at 49.

The record provides no support for this conclusion. Although the Order does not identify the "advanced services technology" to which it is referring, the Company assumes it is Project Pronto. The circumstances surrounding the deployment of Project Pronto are not part of the record in this proceeding. In fact, they post-dated calendar year 2000 when the record was being developed. Thus, Project Pronto cannot be the basis for a negative finding on this statutory goal, nor can it be used to bootstrap a rationale for an investment obligation which is not otherwise supported by the record.

Furthermore, the circumstances surrounding the deployment of Project Pronto are far more complex than this Order acknowledges and do *not* evidence any intent on SBC Illinois' part to withhold technology. As the Commission knows, Project Pronto – and the extent to which the Project Pronto architecture should be unbundled – was the subject of intense litigation in Docket No. 00-0393. The Order's assertion that the Company "chose to suspend deployment" of Project Pronto DSL facilities is unsupported by any evidence in this proceeding, but is an apparent reference to a temporary suspension, which occurred between the issuance of the initial Order and the issuance of the Order on Second Rehearing in Docket 00-0393. As indicated in the Order on Second Rehearing, this temporary suspension of investment occurred because the initial Order required a level of unbundling that threatened the economics of the project. Order on Second Rehearing, Ill. C.C. Dkt. 00-0393 (the "Order on Second Rehearing"); see also Order, Ill. C.C. Dkt. 00-0393 (March 14, 2001). Commissioner Hurley acknowledged in his concurring opinion that, by imposing excessive regulatory burdens on SBC Illinois in the initial Order, the Commission itself had deprived consumers of this new technology for over a year:

> "In its infinite wisdom, this Commission decided SBC's plan was unacceptable. We viewed the Project Pronto proposal as an opportunity to create a variety of new regulatory burdens unknown anywhere else in the country. We decided that it wasn't enough that SBC was already taking on all of the risk with this multi-billion dollar proposal; apparently we also didn't want consumers to get any of the reward." Id. Concurring Opinion of Commission Edward C. Hurley to the Order on Second Rehearing at 1.

The Commission cannot impose a major infrastructure obligation on SBC Illinois because of conduct that stemmed from the Commission's own regulatory decisions in the first place – the logic is entirely circular.

The Commission's second rationale for imposing an infrastructure investment obligation on SBC Illinois rests on its concern that "service quality [be] up to standard." Id. at 211. Investment obligations, however, are not an appropriate mechanism to address service quality issues. There is no necessary connection between any particular level of spending and service quality – and, as noted above, there is certainly nothing in this record that suggests that $1.2 billion over 2006 and 2007 is the "right" number. Moreover, as discussed below, the Commission has ample authority to supervise the service quality directly. As long as SBC Illinois meets its service quality obligations, the Commission should not micromanage how the Company does so. Requiring a carrier to invest capital dollars just for the sake of investing capital dollars is pointless and cannot be related to any legitimate regulatory concern of the Commission under the Public Utilities Act generally or Section 13-506.1 (governing alternative plans of regulation) specifically.

D. THE COMMISSION'S ORDER IS INCONSISTENT WITH ITS PRIOR ORDERS ON INFRASTRUCTURE COMMITMENTS

The Commission's Order also conflicts with its own prior approach to the $3 billion commitment. Beginning with the 1994 Alt Reg Order, the Commission recognized that this commitment was a long-term obligation: in that proceeding, the $3 billion was to be spent over five years, beginning in calendar year 1995. SBC Illinois, however, had no obligation to spend any *particular* amount in any *particular* year: the Company retained the flexibility to spend whatever amounts it deemed appropriate year-by-year, as long as total expenditures totaled $3 billion by the end of 1999 (and they did). The Commission reaffirmed this flexibility when it imposed the new five-year $3 billion investment obligation on SBC Illinois in the Merger Order:

> "(7) Network Infrastructure Investment – AI shall renew and extend the five-year network infrastructure modernization program previously established in its Alt. Reg. Plan. The investment shall total at least $3 billion subject to adjustment in the Commission's subsequent review of the Alt. Reg. Plan. The five-year extension shall commence in the year 2000 or in the first calendar year following the merger closing date. *AI will retain the flexibility to structure and apportion the total network investment over the five-year period.* Merger Order at 240 (emphasis added).

In this Order, the Commission no longer provides SBC Illinois with this flexibility. Instead, the Order requires that $1.2 billion be spent over the *two-year period* 2006-2007, and that $600 million be spent *each year* thereafter, until the Plan is continued or terminated. Order at 212. No rationale is provided for this departure from past orders.

If the Commission imposes an investment obligation on SBC Illinois – which it cannot and should not – at a minimum, it should be structured consistently with the 1994 Alt Reg Order and the Merger Order. The Commission apparently intends that the Merger Order obligation extend at least through 2007 at a *pro rata* level of expenditure. Therefore, the proper approach would be to identify a $4.2 billion total obligation over the entire period at issue ($3 billion for the first five years and $1.2 billion for the last two years, for a total of $4.2 billion). SBC Illinois should be free to structure and apportion this total $4.2 billion network investment obligation over the entire period.

Beyond 2007, the Commission should not attempt to impose any commitment, much less one that is stated on an annual basis. The Commission can initiate a review proceeding whenever it deems appropriate over the next five years. The telecommunications industry is likely to look far different in 2008 than it does today. SBC Illinois doubts that there will be any basis for this Plan at all by 2008, based on the competitive nature of the business at that time. In any event, there is *nothing* in the record in this proceeding that would permit the Commission to guess at what type of regulation, if any, will be appropriate in 2008, much less whether SBC Illinois should be required to invest $600 million per year in its network. Thereafter, as a matter of regulatory practice, the Commission cannot and should not impose specific infrastructure obligations that far into the future.

II. THE ORDER'S RETAIL SERVICE QUALITY PENALTIES ARE EXCESSIVE AND ARE NOT SUPPORTED BY THE RECORD

The Commission should also grant rehearing of its decision to increase the Plan's service quality penalties. The penalties adopted in the Order are excessive, and they are not supported by the record.[6]

The Order increases the service quality penalties for the repair measure (Out of Service Over 24 Hours or "OOS>24") and the installation measure (Installation Within

---

[6] As noted previously, one of the components in the price index is the "Q" factor, which requires additional rate reductions if SBC Illinois' service quality falls below prescribed benchmark levels. The Q factor was adopted in 1994 to guard against any incentive SBC Illinois might have to intentionally degrade service so as to improve its earnings and to satisfy the requirement in Section 13-506.1 that service quality be "maintained" under the Plan. 1994 Alt Reg Order at 58-59. As approved in 1994, the Plan contained eight separate service quality measures. The Commission's Order in this proceeding eliminates some measures and adds others. Order at 164-84. SBC Illinois is not disputing the measures themselves.

Five Business Days) *eightfold.* The original 1994 Alt Reg Order established a Q factor adjustment of 0.25 per missed measure annually, which equates to a $2.65 million permanent rate reduction. In this Order, the adjustment increases to 2.00 for repair and installation, which equates to a *$21 million permanent rate reduction* for any year that the measure is missed. This penalty is imposed on top of a *$30 million penalty* for OOS>24 that was adopted in the Commission's Order approving the SBC/Ameritech merger. Merger Order at 200. Moreover, these penalties are in addition to the other customer credits and penalties imposed by Section 13-712 of the Act and the Commission's Part 730 and Part 732 service quality rules. 220 ILCS 5/13-712; 83 Ill. Admin. Code Parts 730, 732. As a result, the increases in the Q factor are excessive and punitive, and the Commission's conclusion is not supported by the record.

A. THE INCREASE IN THE Q FACTOR IS NOT SUPPORTED BY THE RECORD

During this proceeding, the parties agreed that service quality penalties should be increased if, but only if, it could be shown that existing penalties were insufficient to assure compliance. Thus, the entire debate focused on the sufficiency of the existing penalties. (Am. Ill. Ex. 12.1 at 33-35; Staff Ex. 9.0 at 42-45; GCI Ex. 2.0 at 57). Staff testified that it believed the penalties for the installation and repair measures should be increased because, in Staff's view, those penalties had not created a sufficient incentive for the Company to comply with the Commission's rules. (Staff Ex. 9.0 at 42-43). Staff witness Jackson testified, "The service quality indicator should be sufficiently large to provide the Company with the incentive to meet the minimum requirements." (Id. at 43). Where the existing penalties have provided an adequate incentive, she testified that no increase was justified. (Id. at 45). GCI took a similar position. (GCI Ex. 2.0 at 57).

The Order does not find that the Plan's existing penalties were inadequate, however, and for good reason. In fact, the record did not, and could not, support a finding that existing penalties are insufficient.

Regarding OOS>24, the Company's conduct since 1999 demonstrates that the existing penalties are adequate to maintain reasonable performance. Initially, this measure was subject to the same 0.25 Q factor adjustment as the other service quality components of the Plan. Then, during 1999, the Commission imposed an additional $30 million dollar penalty for OOS>24. As shown by the immense improvement in OOS>24 performance since that penalty was adopted, that incentive has been adequate to insure the Company strives to meet the benchmark. (Am. Ill. Ex. 12.1 at 35). Ameritech Illinois failed to meet this benchmark in 2000 only because of the unforeseen headcount losses that compromised installation and repair service generally — a problem separate from inadequate penalties.

With respect to Installation Within Five Business Days, the Order properly recognizes that the Company has been reporting this measure in the same way as it always has, consistent with the manner used when the original benchmark was developed. As the Proposed Order finds, "the existing benchmark was calculated from data that included vertical services". Order at 170. On that basis, the Company has, without question, met this benchmark consistently over the life of the Plan. To increase this penalty when the Company has *never* missed the current benchmark would be both unfair and inconsistent with the testimony of *all* the parties — that penalties should be increased only if it can be shown that the existing penalties are inadequate. (Am. Ill. Ex. 12.1 at 33-35; see Staff Ex. 9.0 at 42-45; GCI Ex. 2.0 at 57).

Certainly, SBC Illinois recognizes that service quality reached levels that were unacceptable – both to the Commission and to the Company – during 2000. However, the Company's response to that situation demonstrates that greater penalties are not needed to provide the proper incentives. Indeed, as soon as SBC Illinois recognized that headcount had dropped to levels that would not support acceptable performance – long before performance data actually began to decline – management acted to address the situation. That effort included several initiatives.

First, the Company began hiring and training new technicians to restore the balance of force and load. (Am. Ill. Ex. 12.0 at 7-9). The network organization also better equipped its technicians (by deploying new laptop computers and installing Global Positioning Systems in vehicles) and improved and expanded training programs. (Id. at 11-12). The Company also upgraded certain aspects of its network infrastructure that were causing a disproportionate number of trouble reports or installation or repair delays, such as: (1) providing dedicated cable to multi-tenant buildings with high turnover, (2) replacing and upgrading "control points," and (3) improving air pressure systems. (Id. at 12-14). And, specifically to address repair delays, the Company revamped its dispatch and oversight procedures. (Id. at 5-7).

The results of those initiatives are undisputed. The Company's performance improved dramatically. (Am. Ill. Ex. 12.0 at 34-35). Beginning in 2001, SBC Illinois has met *all* of the Commission's service quality benchmarks. See Interim Order, Ill. C.C. Dkt. 02-0240, 13 (June 12, 2002). Indeed, no one questions that SBC Illinois' service is at an all-time high.

SBC Illinois agrees that high quality service is important to its customers. Order at 201. However, based on the record in this case, the Commission should not impose the punitive penalty structure adopted in the Order. SBC Illinois brought its installation and repair performance to its current high level under the *existing* Plan structure and the $30 million repair penalty prescribed in the Merger Order. If these penalties were sufficient – and they were – to provide the desired incentives to the Company to correct any existing service quality problems, then there is no basis for increasing the Plan's penalties at all, much less *eightfold.*

The penalty levels prescribed in the Commission's Order are clearly excessive. In any year that the Company misses the repair standard (OOS>24), SBC Illinois would have to implement a permanent $21 million rate reduction, *plus* a one-time credit of $30 million under the Merger Order. In any year that the Company misses the installation standard (Installation Within Five Business Days), SBC Illinois would have to implement a *$21 million rate reduction.* These penalties dwarf, by *many* orders of magnitude, any penalties automatically assessed on other carriers in Illinois that experience service quality problems.[1] These penalties are directed at a problem that occurred in one year only and which is now three years in the past. There is no continuing pattern of conduct here that could be used to justify these penalty levels, and they cannot be justified based on this record.

---

[1] SBC Illinois is the only carrier operating under an Alternative Regulation Plan. Other carriers in the state are only subject to the Commission's Part 732 Rules, which require customer compensation for missed installation, repair and appointment obligations. Although the Commission may assess civil penalties for violations of its service rules, such penalties are not automatic and must be preceded by notice and hearing. Moreover, the penalties would be in the form of a one-time payment – not permanent rate reductions that cannot be reversed in subsequent years.

The punitive nature of this penalty structure is further exacerbated by the fact that it is triggered by even the slightest error on SBC Illinois' part. For example, for the repair standard, SBC Illinois must restore 95 percent of all out-of-service conditions within 24 hours. If SBC Illinois' performance in a given year is 94.99 percent, instead of 95 percent, the entire $51 million rate reduction would be required. Similarly, with respect to the installation standard, 90 percent of service orders must be completed within five business days. If SBC Illinois completed 89.99 percent of these orders within five business days, instead of 90 percent, the entire $21 million rate reduction would be imposed on the Company. To impose such draconian penalties for what could be very minor infractions is arbitrary and capricious. This is particularly so given that the Company's service is now, and has been for two years, excellent.

The Commission should also consider this penalty structure in light of the signal it sends to the Company. SBC Illinois recognized in 2000 that it needed to take dramatic action to correct a serious decline in its installation and repair performance, and it did so. It is now meeting both the Commission's, and its own, expectations as to the quality of service that should be provided to its customers. To adopt such punitive measures fails to recognize the extraordinary commitment of manpower and capital resources which SBC Illinois has dedicated to service quality over the last two years.

B. THE ORDER FAILS TO CONSIDER THE IMPACT OF SECTION 13-712 OF THE ACT OR PARTS 730 AND 732 OF THE COMMISSION'S RULES

The Order's escalation of the Q factor adjustments also ignores recent changes in the Commission's authority to ensure adequate service quality under Section 13-712 of the Act and the Commission's Part 730 and Part 732 service quality rules, including the revisions to Part 730 that will become effective in the near future. *See* 83 Ill. Admin.

Code Parts 730, 732; October 23, 2002 Order in Ill. C.C. Dkt. 00-0596 ("Part 730 First Notice Order") (issuing first notice on revised Part 730 service quality rules). That authority is not only far greater than it was when the original Plan was adopted, but it is also far greater than it was when the record in this case was closed.

Today, Section 13-712 of the Act and Part 732 of the Commission's rules provide for direct compensation of consumers for installation or repair delays or for missed appointments. 220 ILCS 5/13-712; 83 Ill. Admin. Code Part 732. The Commission has also completed a thorough review of its Part 730 service quality standards, which impose a broad range of service quality measures and benchmarks on all local exchange carriers. See generally Part 730 First Notice Order. Moreover, if SBC Illinois (or any other carrier) violates the Commission's Part 730 or Part 732 rules, Sections 13-303, 13-304 and 13-305 of the Public Utilities Act, all of which were adopted in the 2001 amendments to the Act, permit the Commission to levy civil penalties and, if necessary, to seek injunctions or writs of mandamus. See 220 ILCS 5/13-303, 13-304, 13-305 (effective June 30, 2001).

The Commission's current Part 730 retail service quality rules overlap substantially with the standards in the original Plan, which in fact were originally based on Part 730. 1994 Alt Reg Order at 58; compare 83 Ill. Admin. Code Part 730. The Commission's revised Part 730 rules will resemble the standards proposed in the new Plan even more closely. For example, all four of the measures related to installation and repair, as well as their respective benchmarks, are *identical* in the new Plan and the revised rules.[8] Thus, these rules cover much of the same ground covered by the Plan.

The financial consequences for retail service quality problems can be severe, entirely aside from the retail service quality provisions in the Plan. The civil penalties available to the Commission, adopted in 2001, are substantial. 220 ILCS 5/13-304, 13-305; see also 220 ILCS 5/13-712(c).[9] In addition, SBC Illinois would be subject to penalties applicable under the existing Plan, customer credits pursuant to Section 13-712 and the Commission's Part 732 rules (220 ILCS 5/13-712; 83 Ill. Admin. Code Part 732), and the $30 million merger penalty for Out of Service Over 24 Hours (Merger Order at 244). Clearly, all of these changes have decreased the need for substantial service quality penalties in the Plan and must be considered in the decision making process. In fact, the Order does *not* account for the cumulative impact of these changes and, therefore, is arbitrary and capricious.

Accordingly, the service quality penalty structure imposed in this order should be changed. The evidence in the record supports continuation of the service quality penalty adopted by the Commission in its original 1994 Alt Reg Order, a Q factor of 0.25 for each service quality measure in the Plan. At a minimum, the Q factors for OOS>24 and Installation Within Five Business Days should be reduced substantially. In light of all the

---

8 Out of Service Over 24 Hours (5 percent), Installation Within Five Business Days (90 percent), Business Office Answer Time (60 seconds) and Repair Office Answer Time (60 seconds). Compare Order at 196, 198, 206-08 with Part 730 First Notice Order, App. at §§ 730.510(b)(1), 730.535(a), 730.540(a).

9 The Part 730 First Notice Order does not identify any specific limits on those penalties. Part 730 First Notice Order at 27, App. at § 730.120. SBC Illinois maintains that such penalties must be limited to the amounts set forth in Section 13-305 of the Act. 220 ILCS 5/13-305. However, in either case, the potential penalties are quite significant.

evidence, and considering the Commission's broad authority over service quality independent of the Plan, such changes are entirely reasonable.

III. THE ORDER UNLAWFULLY ATTEMPTS TO INCORPORATE THE WHOLESALE "REMEDY PLAN" THAT WAS ESTABLISHED AS A CONDITION OF MERGER APPROVAL

SBC Illinois also seeks rehearing of the Commission's decision to incorporate here the wholesale performance remedy plan that was established pursuant to Condition 30 of the Commission's Order approving the SBC/Ameritech merger and modified by the Commission in Docket No. 01-0120. SBC Illinois agrees with the Commission's conclusion that the Docket No. 01-0120 plan should not be extended for the life of the alternative regulation plan, and appreciates the opportunity to present an alternative plan for the Commission's consideration in Docket No. 01-0662. Nevertheless, in Docket No. 01-0120, SBC Illinois demonstrated (1) that it would be improper to extend the life of the remedy plan beyond the October 8, 2002 expiration date of the underlying merger condition, and (2) that some of the substantive features of the plan unfairly and excessively penalize SBC Illinois, and fail to recognize SBC Illinois' improvements in wholesale processes and performance. SBC Illinois recognizes that the Commission held otherwise, and those issues are now before the Appellate Court. Because the Order here attempts to transplant the plan from Docket No. 01-0120, SBC Illinois must respectfully renew those objections here.

A. THE REMEDY PLAN WAS ESTABLISHED AS A CONDITION OF MERGER APPROVAL

Pursuant to Condition 30 of the Commission's order approving the SBC/Ameritech merger, SBC Illinois agreed to implement the performance measurements, standards, and remedies used by Southwestern Bell Telephone ("SWBT") in Texas. The "remedies agreed to in the Texas collaborative process" consisted of "liquidated damages" payable to CLECs and "assessments" payable to the State, paid automatically in the event of specified shortfalls in performance. Merger Order at 255-60.

One of the most fundamental elements of Condition 30 was its duration. In the 1999 Merger Order, the Commission unambiguously stated (at 237) that *all* conditions "shall cease to be effective and shall no longer be binding in any respect three years after the Merger Closing Date," unless some different term was "specifically established" in that order. While Staff and AT&T argued that the term of the remedy plan should be indefinite, the order did not "specifically establish[]"a termination date other than the general three-year term specified by the Merger Order and thus, pursuant to the plain language of the Merger Order, it was to expire on October 8, 2002 (three years after the merger closing date). Id.

In its July 10, 2002 Order in Docket No. 01-0120, the Commission ordered SBC Illinois to modify the remedy plan in several substantial respects. SBC Illinois did not and does not object to most of these modifications. However, some aspects of the Commission's order have the effect of unfairly and excessively punishing SBC Illinois even for good wholesale performance. In particular, the Commission ordered SBC Illinois to double all "remedy" payments on individual performance measures, even if it meets a high percentage of performance standards in the aggregate, and even if the individual "misses" are small. Order, Ill. C.C. Dkt. 01-0120, 36-38 (July 10, 2002) (the "Wholesale Remedy Plan Order"). Accordingly, SBC Illinois petitioned for rehearing of the Wholesale Remedy Plan Order, and that order is now before the Appellate Court.

At the same time that it ordered SBC Illinois to modify the remedy plan, the Commission agreed with SBC Illinois that "[t]he only conclusion that can be reached" from the plain language of the Merger Order "is that Condition 30, and consequently the Remedy Plan, expires in three years" from the merger closing date, that is, on October 8, 2002. Wholesale Remedy Plan Order at 20. However, the Commission re-opened Docket No. 01-0120, and without prior notice or hearing, stated (at 3) that the July 10 Order "did not provide for any sunset or automatic termination for that tariffed remedy plan" and that the plan "will apply after October 8, 2002" and "will be available past October 8, 2002 and for the indefinite future until modified in accordance with applicable law." Order on Reopening, Ill. C.C. Dkt. 01-0120, 3 (Oct. 1, 2002). The Order on Reopening is now also before the Appellate Court.

B. THE COMMISSION'S ORDER HERE SEEKS TO TRANSPLANT THE CONDITION 30 REMEDY PLAN

In this docket, Staff and McLeodUSA sought to incorporate the remedy plan from Docket No. 01-0120 into SBC Illinois' alternative regulation plan, so as to circumvent the October 2002 termination date of the merger condition. The Commission correctly "disagree[d] that the 01-0120 Remedy Plan should remain in effect as long as SBC Illinois has an alternative regulation plan." Order at 190. Nevertheless, the Commission held "the 01-0120 Remedy Plan to be the most thorough and complete alternative at this time" and "deem[ed] the 01-0120 Remedy Plan effective up to and until a wholesale performance measure plan for Section 271 purposes is approved by this Commission." Id. The Commission has since confirmed that SBC Illinois will have the opportunity to present a modified, alternative plan for the Commission's consideration in Docket No. 01-0662, the ongoing investigation into SBC Illinois' compliance with section 271 of the federal Telecommunications Act of 1996.

C. THE COMMISSION SHOULD GRANT REHEARING AND REVERSE ITS ORDER WITH RESPECT TO THE REMEDY PLAN

While SBC Illinois greatly appreciates the opportunity to present an alternative remedy plan, it respectfully disagrees with the Commission's decision to extend the term of the Docket No. 01-0120. For the following reasons, the Commission should not incorporate the remedy plan from Docket No. 01-0120.

First, there is no evidentiary record or showing of need to support the Commission's order. There is no evidence in this record of any current problem with wholesale service quality, and even the CLECs did not allege one. The record in Docket No. 01-0120 does not fill the evidentiary gap here. The evidentiary record in that Docket was closed in 2001, and it did not include wholesale performance data after December 2000. Much has happened since then, including SBC Illinois' implementation of numerous enhancements to electronic systems and processes as a result of the other conditions of the merger, and as a result of the third-party test of its operations support systems. Thus, the record does not include nearly two years of operational improvements and highly relevant performance data. Imposing monetary sanctions on such an outdated record cannot be justified. In any event, no part of the record in Docket No. 01-0120 was ever incorporated into the record in this proceeding, so that record could not possibly support the Commission's Order here. 220 ILCS 5/10-103.

Second, the orders in Docket No. 01-0120 were not based on – and did not even consider – the standards for an alternative regulation plan under Section 13-506.1 of the PUA. Instead, Docket No. 01-0120 *only purported to apply the standards for Condition* 30 of the merger approval. It would be improper to simply transplant that decision here.

Third, the bottom-line effect of the Commission's order here is to extend the duration of Condition 30, under which SBC Illinois implemented the performance "remedy plan" used by its affiliate (SWBT) in Texas. But the duration of that plan was long since established by the plain terms of the Merger Order, which states (at 237):

> Except where other termination dates are specifically established, all conditions set out below shall cease to be effective and shall no longer be binding in any respect three years after the Merger Closing Date.

The Merger Order does not "specifically establish" any other termination date for the remedy plan. Thus, by the unambiguous terms of the Merger Order, the remedy plan was to "cease to be effective and shall no longer be binding in any respect" on October 8, 2002, three years after the Merger Closing Date of October 8, 1999.

Condition 30 thus expired over three months ago. As SBC Illinois demonstrated above with respect to Condition 7, the Commission is estopped from altering the termination date of the remedy plan. After representing, in the Merger Order, that merger approval required SBC Illinois to implement Condition 30 for a limited term of three years, the Commission is not free to unilaterally alter that term.

As also shown above, the Illinois Public Utilities Act provides a further bar against extension of the remedy plan. Section 7-204(f) of the Act (under which the Commission imposed Condition 30 in the Merger Order) authorizes the Commission to impose "terms, conditions or requirements" *only* "[i]n approving any proposed reorganization pursuant to this Section." Section 7-204 by its plain terms applies only when a proposed reorganization is pending. It precludes the Commission from imposing new conditions after a reorganization has been consummated.

Fourth, as SBC Illinois demonstrated in Docket No. 01-0120, two of the principal substantive features of the plan adopted in Docket No. 01-0120 – namely, the Commission's across-the-board doubling of remedy amounts, and its elimination of the K table, a statistical tool designed to prevent the imposition of remedies based solely on random variation – are arbitrary, and unfairly penalize SBC Illinois for good performance. Wholesale Remedy Plan Order at 21, 35.

Finally, for the reasons described above, SBC Illinois has appealed from the Commission's orders in Docket No. 01-0120. Simply put, it would be improper to impose a plan here for the sole purpose of circumventing a court decision that might hold the exact same plan to be unlawful.

IV. THE PLAN'S BASKET STRUCTURE SHOULD BE SIMPLIFIED

Under the terms of the original Plan, noncompetitive services were divided into four baskets. The four baskets consisted of the following: (1) a Residence basket, which contained residence access lines and usage; (2) a Business basket, which contained business access lines, usage, and discretionary services; (3) a Carrier basket, which contained switched access, special access, cellular access and various other carrier services; and (4) an Other basket, which contained directory services; operator services; payphones; private lines; discretionary residence services, such as features like call waiting; optional calling plans; and residence nonrecurring charges.[10] 1994 Alt Reg Order at 66, 69; Am. Ill. Ex. 1.0, Sch. 1 at 10. The baskets were structured to ensure that

[10] Over the first five years of the Plan, many of these services were declared competitive and removed from the Alternative Regulation Plan (*e.g.*, local toll usage – both business and residence – special access, directory services, operator services, payphones, private line services, various business services and so forth. This progression of services from noncompetitive to a competitive classification was expected when the 1994 Alt Reg Order was adopted. As a result, today, residence nonrecurring charges, vertical features and optional calling plans comprise 90 percent of what is in the Other basket. (Am. Ill. Init. Br. on New Legislation at 12).

all customer classes benefited equally from price regulation, and, with respect to the splitting of residence services between the Residential and Other baskets, to facilitate the application of the five-year rate cap to basic network access lines and usage. 1994 Alt Reg Order at 69. The Business basket disappeared as a matter of law in 2001, when all business services were declared competitive in Section 13-502 of the Act. This left the Residence, Carrier and Other baskets. SBC Illinois has recommended throughout this proceeding that these baskets be consolidated, or, at a minimum, that the Residence and Other baskets be combined. (Am. Ill. Init. Br. at 44-45).

The Commission's Order retains the Residence, Carrier and Other baskets going forward and adds a new "Packages" basket. Order at 116-18. The "Packages" basket is a response to new Section 13-518 of the Act, where the legislature mandated the creation of packages which include calling services (usage) and/or features (*e.g.*, Call Waiting and Caller I.D.). The legislative package which includes only usage was assigned to the Residence basket, while the two legislative packages which include usage and features were assigned to the new Packages basket. On a going forward basis, all packages of services which include features are to be assigned to this basket. Order at 116-19. The Commission also reassigned certain optional calling plans (*e.g.*, the SimpliFive and Call Pack plans) from the Other basket to the Residence basket. Id.

This approach to the basket structure is not viable over the long run. The only services in the Residence basket today are network access lines and local usage (Bands A and B). At best, residence network access lines are priced very close to cost, and may be below cost based on current studies.[11] (Am. Ill. Ex. 1.2 at 8-9, 17; Am. Ill. Ex. 9.0 at 5-7). Rate reductions would be inconsistent with the terms of the Plan and long-standing Commission rate design policies. (1994 Alt. Reg Order, Attachment A, par. I.A.2(g); Am. Ill. Ex. 1.2 at 15-22; Am. Ill. Ex. 1.3 at 139). This leaves only Bands A and B usage, which have been the subject of many years of rate reductions already. The Commission cannot continue to expect local usage rates to bear the entire brunt of the Company's pricing obligations in this basket.

Consolidating the Residence, Other and Packages baskets will provided needed flexibility without compromising the Commission's concern that all customer groups benefit from the Plan. Since all three baskets contain only residence services, residence customers will benefit from reductions in any of the included services. For example, residence non-recurring charges ("NRCs") required to install new service or modify existing service are assigned to the Other basket. Reductions in these NRCs make it easier for customers to obtain service and could improve overall subscriber levels in SBC Illinois' service territory. (Am. Ill. Ex. 9.0 at 9; Tr. at 2162). Features like custom calling services are popular with customers and have relatively high margins. By mandating packages in Section 13-518, the legislature has recognized that features are part and parcel of the overall service which customers expect today and rendered obsolete the line which the 1994 Alt Reg Order drew between "core" and "discretionary" services.[12]

---

[11] These studies were the subject of considerable dispute in the proceeding. Since SBC Illinois withdrew its rate rebalancing proposal after the 2001 amendments to the PUA, these disputes were never resolved. Order at 91-92.

[12] As noted above, this line was drawn primarily so that a price cap could be imposed on the Residence basket only. The price cap expired in 1999 and has not been renewed in this Order.

The Order rejects consolidation of the Residence and Other baskets and mandates creation of the Packages basket on the grounds that SBC Illinois might "manipulate" the prices in an expanded Residence basket by decreasing the prices on high margin services (like features) in order to increase the price of inelastic services (like network access lines). Order at 117-18. This is a fundamental misconception that has plagued all of the analyses of this basket issue – first by GCI/City, then by the Administrative Law Judges and now by the Commission. SBC Illinois *cannot* manipulate prices in this manner. The Plan has strict rules on price changes. Rate increases that exceed the percent change in the PCI plus 2 percent were prohibited in the 1994 Alt Reg Order and continue to be prohibited under the Commission's recent Order. Order at 105. Because the index has always been negative (by 2 percent or more), the Company has had *no* opportunity to increase any rate under the Plan since 1994. (Am. Ill. Ex. 1.1 at 43-45). This is undisputed. Even if inflation increased dramatically, any rate increases would be limited to a maximum of 2 percent.[13] If SBC Illinois were to propose such an increase, it would be the subject of debate and Commission review in the annual filing proceeding and could be disapproved if the Commission found it to be inappropriate. See e.g., June 26, 1996 Order, Ill. C.C. Dkt. 96-0172 at 11-13. In short, SBC Illinois *cannot* raise rates unilaterally, and this concern about price manipulation cannot be the basis for requiring three baskets.

The Order also suggests that SBC Illinois could frustrate the legislative intent that the mandated packages produce savings for the "average" customer by raising prices for packages and reducing prices for features. Order at 118. Again, the Company cannot

[13] For example, the average price of an SBC Illinois network access line statewide is $11.81. (Am. Ill. Ex. 1.3 at 147). A 2 percent increase would be $.22. This is hardly the cause for alarm and is not a sound basis for balkanizing residence services among *three* separate baskets.

increase these prices in the way the Order suggests. Furthermore, SBC Illinois' prices for the mandated packages must continue to meet the requirements of Section 13-518, regardless how the baskets are structured. In other words, Section 13-518 operates as a separate constraint on SBC Illinois' pricing flexibility, above and beyond the other pricing limitations in the Plan, and it is not inconsistent with basket consolidation.

Finally, continued pressure to reduce rates in the Residence basket as it exists today is counterproductive over the long run: it simply encourage competitors to seek out and serve communications intensive households and to ignore customers who make less use of the network. (Am. Ill. Ex. 1.3 at 134; Am. Ill. Ex. 4.1 at 6-7). Whatever one's view of the merits of increasing the prices for local service, continuing to require *decreases* will not promote this Commission's procompetitive policies. In addition, at some point, the Company will hit price floors for the services in the Residence basket (*i.e.*, LRSIC and/or imputation). From an economic perspective, social welfare will be maximized if the Company has more freedom to take a larger proportion of any required rate reductions on higher margin services, such as those in the Other and Packages basket. (Am. Ill. Ex. 4.1 at 22). These critical policy issues are ignored completely in the Commission's Order.

V. THE API/PCIs SHOULD NOT BE REINITIALIZED

The rate reductions s required each year under the Plan are determined by the changes in the price cap index ("PCI") in relation to the actual price index ("API") for the services in any given basket. The PCI is calculated each year and the same PCI is applied to each basket under the Plan. An API is separately calculated for each basket and reflects the price changes that actually took place over the year (or prior years) in that basket. Both the PCI and the API were set at 100 when the Plan was adopted in 1994 and have been declining since then with each annual filing. (Staff Ex. 13.0 at 6-7, 9).

Under the Plan, the API must be equal to or lower than the PCI. 1994 Alt Reg Order, Attachment A, par. I.A.2(c). To understand how this process works in practice, assume that the PCI for the current Plan year was 85 percent and the PCI for the next Plan year is 83 percent, and that the API in all baskets is 85 percent. SBC Illinois would have to implement rate reductions in each basket effective July 1, so that the API equals 83 percent. Assume, however, that in one basket SBC Illinois had already reduced rates as part of a marketing initiative or for some other reason, such that the API was only 83 percent. No rate changes would be require in that basket that year, because ratepayers subscribing to those services *had already received the rate reductions to which they were entitled.*

The Commission's Order concludes that the API/PCI should be reinitialized to 100 as part of this review process. Order at 119. The effect of this requirement is to erase the effect of all rate changes which have occurred since 1994. The stated rationale is to "maximize the efficiency gains to be passed along to customers." Id. As shown below, in fact it does no such thing. It simply rewards one group of customers – the long distance carriers – with a financial windfall that they have done nothing to deserve and that is totally unsupported by the record.[14]

The long distance carriers have been the beneficiaries of massive rate benefits since 1994, far in excess of any other customer group. Carrier rates declined significantly as a result of rate policies adopted by the Federal Communications Commission ("FCC")

---

[14] The Carrier basket is the only basket in which there is a significant gap (often referred to as "head room") between the PCI and the API. Therefore, carriers are the only beneficiaries of this requirement of the Order.

for interstate carrier access rates, which were then mirrored in Illinois under the Commission's "mirroring" policies in Docket No. 83-0142. (Staff Ex. 13.0 at 21-22). Then, in 2000, in Docket Nos. 97-0601/0602/0516, the Commission required that intrastate switched access rates be set *at* LRSIC, plus a 28.86 percent common overhead allocation. Order, Ill. C.C. Dkts 97-0601 et al., 48-49 (March 29, 2000). This resulted in an overall rate reduction of over $33 million annually to the IXCs. (Am. Ill. Ex. 9.0 at 14). Due to the combined effect of these FCC- and ICC-mandated rate changes, rates in the Carrier basket are now far below the level which otherwise would have been required by the Plan. For example, in last year's annual price cap filing, SBC Illinois calculated the Residence, Carrier and Other baskets' APIs as follows:

Residence Services	85.0171
Carrier Basket	57.5372
Other Services	85.0180

In other words, carriers' rates have been slashed by almost 50 percent since 1994 (with a PCI of 57 percent), while residence customers' rates have declined by approximately 15 percent (with APIs of 85 percent). Interim Order, Ill. C.C. Dkt. 02-0240 at 13-14 (June 19, 2002).[15]

If the Commission now reinitializes all API/PCIs at 100, the only effect will be to flow yet *more* rate reductions in the direction of the IXCs – as if the events of the 1994-2002 period had never happened. There is no policy rationale for such preferential treatment of a customer group that has already been treated very well indeed.

The Commission's Order attempts to justify this regulatory munificence on the grounds that it will "restore the ability of the Plan to maximize the efficiency gains to be

15 Because the Commission rejected SBC Illinois' exogenous change proposal, the PCI (and, therefore, the APIs) had to be recalculated in the compliance filing in June. Id. at 10-12, 17 (Findings (4)-(6), (10) and the first ordering paragraph).

passed along to customers." Order at 119. However, the Plan never stopped passing efficiency gains along to customers and nothing needs to be "restored." The IXCs not only received their full share of SBC Illinois' efficiency gains over the period 1994-2002, but they also received a cash advance on SBC Illinois' efficiency gains through approximately *2014*. They simply received these future benefits up front in immediate rate reductions, rather than gradually over time through the annual price cap filings.[16] (Am. Ill. Ex. 1.3 at 89-90). There is neither a record nor a policy basis for rewarding the IXCs with yet *more* rate reductions on a year-to-year basis.

The Commission's Order raises the spectre of SBC Illinois using this "headroom" in the Carrier basket "for the purposes of future rate increases." Id. at 119. This again reflects a fundamental misunderstanding of the workings of the Plan. As explained previously, the Company has no realistic ability to raise *any* rates. Furthermore, there are no services of any consequence in the Carrier basket whose rates could be increased: wholesale (resale) prices are established by rate formulas that cannot be changed absent another wholesale (resale) pricing proceeding and carrier access rates are capped by the pricing rules established in Docket Nos. 97-0601/0602/0516. If there is any confusion on this issue, the Company's objective here is *not* to raise carrier rates. SBC Illinois' objective is to avoid having to reduce carrier access rates beyond what was ordered in Docket Nos. 97-0601/0602/0516, and provide a windfall to the IXCs and to the IXCs alone. Reinitializing the PCI/APIs as proposed in the Order would unreasonably advantage carriers, contrary to the dictates of Section 13-506.1(b)(7) of the Act.

[16] As shown by the chart, the spread between the Residence/Other baskets and the Carrier basket is approximately 27 percentage points. The PCI typically declines about 2-3 percentage points per year. (Tr. at 2114). If the 27 percentage point spread is allocated over future years at approximately 2.5 points per year, it will be 11 years before this "cash advance" is used up.

Finally, the Order cites with approval arguments made by Staff and GCI/City that the "headroom" in the Carrier basket results from "actions outside the Plan." Order at 119. This is a policy *non sequitur*. The Plan only requires that customer groups receive the rate reductions to which they are entitled under the index. It does not matter whether prices result from the annual filing process, from rate actions taken independently by SBC Illinois over the course of a Plan year, or regulatory actions by this Commission or the FCC. A rate reduction is a rate reduction. If the API is lower than the PCI, nothing further is required to ensure that the Plan's benefits have been flowed through to customers.

CONCLUSION

For all of the reasons set forth herein, SBC Illinois respectfully requests that the Commission grant hearing in order to modify its Order as recommended herein.

Respectfully submitted,

ILLINOIS BELL TELEPHONE COMPANY

By: ______________________
One of Its Attorneys

Louise A. Sunderland
Karl B. Anderson
Mark A. Kerber
Illinois Bell Telephone Company
225 West Randolph, Floor 25D
Chicago, IL 60606
312/727-6705
312/727-2928
312/727-7140

CERTIFICATE OF SERVICE

I, the undersigned, certify that a copy of the foregoing document was served on the parties on the attached service list by electronic transmission and by U.S. Mail on January 29, 2003.

Mark A. Kerber

SERVICE LIST FOR ICC DOCKET NO. 98-0252/98-0335/00-0764

Philip Casey
Illinois Commerce Commission
160 North LaSalle Street, Suite C-800
Chicago, IL 60601-3104
pcasey@icc.state.il.us

Eve Moran
Illinois Commerce Commission
160 North LaSalle Street, Suite C-800
Chicago, IL 60601
emoran@icc.state.il.us

Jack Pace
City of Chicago
30 North LaSalle Street, Suite 900
Chicago, IL 60602
jpace@ci.chi.il.us

Patrick N. Giordano
Giordano & Neilan, Ltd.
333 North Michigan, Suite 2800
Chicago, IL 60601
patrickgiordano@dereglaw.com

Calvin Manshio
Manshio & Wallace
4753 North Broadway, Suite 732
Chicago, IL 60640
calpeg@worldnet.att.net

Henry Kelly, Joseph E. Donovan
O'Keefe, Ashenden, Lyons & Ward
30 North LaSalle Street, Suite 4100
Chicago, IL 60602
henrykelly@okeefe-law.com
josephdonovan@okeefe-law.com

Owen E. MacBride, Terri Brieske
Schiff Hardin & Waite
233 South Wacker Drive
6600 Sears Tower
Chicago, IL 60606
omacbride@schiffhardin.com
tbrieske@schiffhardin.com

Robert J. Kelter
Citizens Utility Board
208 South LaSalle, Suite 1760
Chicago, IL 60604
rkelter@cuboard.org

Matthew L. Harvey
Illinois Commerce Commission
160 North LaSalle Street, Suite C-800
Chicago, IL 60601
mharvey@icc.state.il.us

John E. Rooney
Sonnenschein Nath & Rosenthal
800 Sears Tower
233 South Wacker Drive
Chicago, IL 60606
jrooney@sonnenschein.com

Michael Ward
Michael W. Ward, P.C.
1608 Barclay Blvd
Buffalo Grove, IL 60089
mwward@dnsys.com

Dennis Muncy, Joseph Murphy
Matt Deering
Meyer Capel
306 West Church Street
P.O. Box 6750
Champaign, IL 61826
dmuncy@meyercapel.com
jmurphy@meyercapel.com
mdeering@meyercapel.com

Allan Goldenberg, Mark N. Pera,
Marie Spicuzza, Ann Bloss
Cook Co. State's Attorney's Office
69 West Washington, Suite 700
Chicago, IL 60602
agolden@cookcountygov.com
mpera@cookcountygov.com
saopib@wwa.com
abloss@cookcountygov.com

Cheryl Urbanski Hamill
AT&T Communications
222 West Adams Street, Suite 1500
Chicago, IL 60606
chamill@att.com

Darrell S. Townsley
WorldCom
205 North Michigan Ave, 11th Floor
Chicago, IL 60601
darrell.townsley@wcom.com

Peter Nyce, Jr.
Department of the Army
Office of the Judge Advocate General
901 North Stuart Street
Arlington, VA 22203
peter.nyce@hqda.army.mil

Susan L. Satter
Illinois Attorney General's Office
100 West Randolph Street, 11th Floor
Chicago, IL 60601
ssatter@atg.state.il.us

Brian Rankin
XO Illinois, Inc.
303 East Wacker, Concourse Level
Chicago, IL 60601
brankin@nextlink.com

Clyde Kurlander
Lindenbaum, Coffman, Kurlander
Three First National Plaza
70 West Madison Street, Suite 2315
Chicago, IL 60602
ckatlantis@aol.com

Richard M. Rindler
Swidler Berlin Shereff & Friedman
3000 K Street NW, Suite 300
Washington, DC 20007
rmrindler@swidlaw.com

David Woodsmall
MGC Communications, Inc.
3301 North Buffalo Drive
Las Vegas, NV 89129
gwoodsmall@mgcicorp.com

Kent F. Heyman
MGC Communications, Inc.
171 Sully's Trail, Suite 202
Pittsford, NY 14534
kheyman@mgcicorp.com

Carol P. Pomponio
XO Illinois, Inc.
303 East Wacker, Concourse Level
Chicago, IL 60601
cpomponio@xo.com

Stephen D. Minnis
Sprint Communications
6450 Sprint Parkway
KSOPHN0214-2A571
Overland Park, KS 66251
steve.minnis@mail.sprint.com

Thomas Rowland
Rowland & Moore
77 West Wacker Drive
Suite 4600
Chicago, IL 60601
tom@telecomreg.com

Brett D. Leopold
Sprint
6450 Sprint Parkway
KSOPHN0212-2A461
Overland Park, KS 66251
brett.d.leopold@mail.sprint.mail